

Influence of Manipulated Tax System on Aggressive Accounting Practices: Evidence from Stakeholders in South-East, Nigeria

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Abstract: *Aggressive accounting is carried out with an objective of making the company appear to be financially stronger or weaker depending on the management's aspirations. This practice is considered professionally unethical in Nigeria even though in some countries it's permitted by law. Thus, the study is set out to examine tax avoidance and evasion as factors influencing aggressive accounting practice in Nigeria. The researcher collected and analyzed data from respondent at Federal Inland Revenue Service, state tax authorities in the south eastern zone and professional accountants working for various companies in Nigeria. The propositions made were tested using descriptive statistical method. The results of the study established that tax avoidance and evasion is indeed one of the major factors contributing to practice of aggressive accounting among companies in Nigeria. Evidence also reviews a positive relationship between the Nigerian tax administration and aggressive accounting. Based on the above, it was recommended that among others that professional bodies should make laws which reduce the chances of alternative accounting methods.*

Keywords: *Influence, Tax Avoidance and Evasion, Creative Accounting, Stakeholders, South-East, Nigeria.*

1. INTRODUCTION

Current accounting practices allow a degree of choice of policies and professional judgment in determining the method of measurement, criteria for recognition, and even the definition of the accounting entity. The exercise of this choice can involve a deliberate non-disclosure of information and manipulation of accounting figures, thereby making the business appear to be more profitable (or less profitable for tax purposes) and financially stronger than its supposed to be (Ijeoma, 2014). With this practice, users of accounting are being misled and this constitutes a threat to corporate investment and growth. Aggressive accounting techniques permits corporations to report financial results that may not accurately portray the substance of their business activities. In the light of this, Nigeria House of Representatives (2013) discovered in their preliminary investigation that some organisations portray poor quality of returns, discrepancy in data collected, outright refusal to present documentary evidence, blanket violations of existing laws, self exemption from existing rules, false declaration, manipulation and distortion of information among others. It was in this regard that Jibrin (2013) stated that:

The balances reported in the published audited accounts of some banks showed huge variance with the figures submitted to the committee. The data submitted by the Central Bank of Nigeria in their monthly returns on the same issues was found to be different from what was tendered before the committee. Even more embarrassing are the inconsistency and huge variances in some data provided in different pages of documents submitted, then leaving the committee to conclude that many banks blatantly engage In creative accounting technique of inflating their operating cost to reduce their exposure to taxes.

However, what accounted for this development was an ambitious desire by firms was to avoid tax payments. This is why Malkani, and Haloush, (2008) observe that tax evasion is perpetrated through acts such as presenting incorrect statement of accounts, making false entries or alterations, or false books or records, destruction of books or records, concealment of assets or covering up sources of

income constitute tax evasion. Aggressive accounting is thus influenced by tax avoidance which arises in a situation where the taxpayer arranges his financial affairs in a way that would make him pay the least possible amount of tax without infringing the legal rules. Predicted on this development, (Amat and Gowthorpe, 2010) noted in their study that tax is one of the major motivators of aggressive accounting since it is based on the business income.

Tax evasion in most developing countries is so rampant and the scenario is much worsened by the fact not many of these governments have made an effort to measure the ethical reasons that tax payers give, the extent of this problem and at the same time its impact. Hence, when required revenue for smooth operation cannot be raised, these countries offer resort to increase tax rates or borrowing which may not only crowd out the private sector of their economies but also lead them to debt traps (Chiumya, 2006). Aggressive accounting are not practiced openly; firms practice them for different intentions and this is why Ayala and Giancarlo (2006) observed that users of accounting information seem not to have perceived this practice of aggressive accounting which has led to collapse of many companies globally such as Enron and World Com and locally such as Levers Brothers, Cadbury Plc etc.

Closer home, tax evasion and avoidance had robbed the Nigerian government of substantial tax revenue. According to the Nigerian Stock Exchange, 85 percent of corporate tax revenue in the country accrues from the 196 companies listed on the exchange compared to the 30,000 companies registered with the Corporate Affairs Commission. This is a serious indictment of the administrative machinery and capacity of the tax authorities in Nigeria (Sosanya, 1981).

Beside this, revenue derived from income taxes has been grossly understated due to improper tax administration arising from under assessment and inefficient machinery for collection (Ola, 2001; Oluba, 2008; Adegbe and Fakile, 2011) as cited by Okafor (2012). Although tax evasion and avoidance are problems that face every tax system, the Nigerian situation seems unique when viewed against the scale of corrupt practices prevalent in Nigeria (Adebisi and Gbegi, 2013). With increasing hard economic times; companies may be motivated to practice aggressive accounting for diverse reasons. Players in the accounting profession may not fully understand the operations of aggressive accounting because different companies practice aggressive accounting for different reasons (Kamau, Mutiso and Ngui, 2012). In the light of this, the question we often ask ourselves is: do tax avoidance and evasion have any significant relationship on aggressive accounting in Nigeria? Predicated on this, the researcher formulated the following hypotheses to guide the study:

Ho: There is no significant relationship between tax avoidance and evasion and aggressive accounting in Nigeria

Ho: The Nigerian tax system does not influence aggressive accounting

The rest of the papers is organized as follows: Section one includes in introduction and formulated hypotheses under investigation. Section two involves the review of related literature. Section three includes research designs and methodologies. Section four shows the data presentation, analysis and interpretation; while section five embraces study findings, conclusion and recommendations.

2. REVIEW OF RELATED LITERATURE

2.1. The Relationship between Tax Avoidance and Evasion and Aggressive Accounting

Tax evasion and avoidance have adverse effect on government revenue. Tax avoidance generates investment distortion in the form of the purchase of assets exempted from tax or under-valued for tax purposes. Avoidance takes the form of investment in arts collection, emigration of persons and capital. And as observed by Toby (1983) the taxpayer indulges in evasion by resorting to various practices. These practices erode moral values and build up inflationary pressures. This point can be buttressed with the fact that because of the evasion of tax, individuals and companies have a lot of money at their disposal. Companies declare higher dividends and individuals have a high take home profit. This increase the quantity of money in circulation but without a corresponding increase in the goods and services. This then build up what is known as inflationary trends where large money chases few goods (Toby, 1983).

Simser (2008) as cited by Kamau, Mutiso and Ngui (2012) elucidates that taxpayers are required to pay taxes based on accounting and legal advice provided which should be aligned to the firm's financial reports and the existing tax rules. Taxation is complex and exploring the tax system requires

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the guidance of skilled lawyers, accountants and other advisors. Tax evasion is unacceptable and/or illegal while tax avoidance is perfectly acceptable however there is no clear line between the two. This is the dilemma that is faced by the advisors. Tax evasion is perpetrated through acts such as presenting incorrect statement of accounts, making false entries or alterations, or false books or records, destruction of books or records, concealment of assets or covering up sources of income constitute tax evasion (Malkani, and Haloush, 2008). It is in the light of this, that tax evasion and avoidance can arguably be said it provokes aggressive accounting practices in firms because it is based on business income (Amat and Gowthorpe, 2012; Balacil and Pop, 2008; Niskanen and Keloharju, 2000; and Hermann and Inoue, 1996).

2.2. The Influence of Nigeria Tax Administration on Aggressive Accounting

The real causes of aggressive accounting lie in the conflicts of interest among different interest groups (government). Managing shareholder's interest is to pay less tax and dividends. Investor-shareholders are interested to get more dividends and capital gains. Country's tax authorities would like to collect more and more taxes. Employees are interested to get better salary and higher profit share. This development enables aggressive accounting to put one group or two at advantage position at the expense of others.

The Nigerian tax system has been based on 1948 British tax laws and has been undergoing a lot of changes. Since then, different governments have continued to improve on Nigeria's taxation system. A vital aspect of the improvement on the nation's tax system is the recent Federal Inland Revenue Service (Establishment) Act, 2007, Companies Income Tax (Amendment) Act, 2007 and the Draft National Tax Policy pending before the National Assembly (Fagbemi, Uadiale and Noah, 2010).

This agency created by these reforms invariably is charged with the task of tax administration in Nigeria. Unfortunately, clients have cried for unfair treatment in tax computation and this is why Sanni (2005) noted that any vibrant tax system will have the following "tripod"; Tax Policy, Tax Law and Tax Administration. He mentioned that a tax system is administered through tax policies while the tax laws serve as the legal backing. Soyode and Kajola (2006) noted some of the sources of tax laws in Nigeria to include Legislations, Constitution, Court judgment and Circulars. For example, Personal Income Tax Act (1993) *as amended* (in respect of Pay-As-You-Earn and Direct Taxation: Self-Assessment) is a typical legislative source of tax laws in Nigeria. (Sanni, 2005; Soyode and Kajola, 2006); PITA, 1993 *as amended*.

3. METHODOLOGY AND RESEARCH DESIGN

The study adopted a descriptive survey design which the paper believes will unravel the critical elements or characteristics under investigation.

A population of 1991 respondents which consist of senior management staff of federal and state tax authorities and members of the Chartered Accountants or Association of National Accountants of Nigeria (ANAN) and Institute of Chartered Accountants of Nigeria (ICAN) respectively across the five states of Abia, Anambra, Ebonyi, Enugu and Imo states in the south-east, Nigeria.

Table 3.1.1. *Distribution of Staff by Geographical Location*

FIRS:	TOP MGT. STAFF	SBIR:	TOP MGT. STAFF
ABIA	42	ABIA	33
ANAMBRA	37	ANAMBRA	28
EBONYI	28	EBONYI	19
ENUGU	54	ENUGU	44
IMO	47	IMO	31
TOTAL	208	TOTAL	155
ACCOUNTANTS/AUDITORS	ANAN	ACCOUNTANTS/AUDITORS	ICAN
ABIA	178	ABIA	143
ANAMBRA	217	ANAMBRA	179
EBONYI	97	EBONYI	72
ENUGU	256	ENUGU	188
IMO	107	IMO	191
TOTAL	855	TOTAL	773

Source: *Staff List of FIRS/State Authorities and Membership Registers, 2014*

3.1. Sampling And Sampling Technique

In determining the sample size of the study, Taro-Yamene (1964) formula for finite population was applied.

$$n = \frac{N}{1 + N * (e)^2}$$

$$N = \frac{1991}{1 + 1991 * (.05)^2} = 333.1 \text{ (Approx 333)}$$

Bowley's proportional allocation formula was adopted to determine the number of units to be allocated to each stratum:

$$N_h = \frac{nN_h}{N}$$

Where in:

H = number of units allocated to each stratum.

N = total sample size

Nh = number of items in each stratum in the population.

For FIRS: $nh = \frac{333 \times 208}{1991} = 34$

For SBIR: $nh = \frac{333 \times 155}{1991} = 26 \text{ (approx)}$

For ANAN: $nh = \frac{333 \times 855}{1991} = 143$

For ICAN: $nh = \frac{333 \times 773}{1991} = 129$

3.2. Results and Discussions

Descriptive Statistics of Questionnaire:

The following descriptive statistics were computed: Mean (a measure of central tendency) and standard deviation (a measure of dispersion)

Table3.2.1. Mean and Standard Deviation

	N	Mean	Std. Deviation
Aggressive accounting is practiced in a bid to encourage tax avoidance	240	3.8966	.44681
Aggressive accounting is practiced in a bid to encourage tax evasion	240	3.7759	.53124
Managers in a bid to reduce the amount of tax to be paid manipulate the financial statement	240	3.8966	.61243
The tax system or administration in Nigeria influence the way in which accountant prepares financial statement	240	3.9655	.72464
The inflation of expenses reduce the amount being paid to tax authorities	240	3.9483	.60473
Companies destroys books of records in order to evade tax payment	240	3.8276	.53436
The loopholes in the legal regulatory framework of Nigerian tax system promotes tax avoidance and encourages aggressive accounting in manufacturing companies	240	3.7586	.57156
The loopholes in the accounting regulatory framework of Nigerian tax system promotes tax avoidance and encourages aggressive accounting in manufacturing companies	240	3.7931	.55436
The achievement of internally set corporate targets promotes aggressive accounting by encouraging tax avoidance in Nigerian manufacturing companies	240	4.0172	.43895
Meeting external expectations by companies promotes aggressive accounting by encouraging tax avoidance in Nigerian manufacturing companies	240	3.8621	.60548
Aggressive accounting practice in Nigerian manufacturing companies is done with the aim of manipulating share price	240	3.7586	.62996
Valid N (listwise)	240		

Source: SPSS Ver. 22

The table above showed that all questions had mean (average) scores greater than 3.5 respectively.

3.3. Questionnaire Reliability Test

Cronbach alpha the coefficient of internal consistency was computed using SPSS Ver. 22. The reliability result is shown in the table below:

Reliability Statistics	
Cronbach's Alpha	N of Items
.848	11

Source: SPSS Ver. 22

Alpha showed a value of .848, a strong indicator of internal consistency.

Test of Hypotheses

Hypothesis One

H₁: There is a relationship between tax avoidance and evasion and aggressive accounting

Descriptive Statistics: Hyp1

Variable	N	N*	Mean	SE Mean	StDev	Minimum	Q1	Median	Q3
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Hyp1	58	0	3.8728	0.0487	0.3706	3.1250	3.7188	3.8750	4.0000
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Variable Maximum

Hyp1	5.0000
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Source: Minitab ver. 16

The descriptive statistics shows that the grand mean score of the questions used in testing this hypothesis was 3.8728 (approx 3.9) One-Sample Z

Test of mu = 2.5 vs not = 2.5

The assumed standard deviation = 0.3706

N	Mean	SE Mean	95% CI	Z	P
58	3.8728	0.0487	(3.7774, 3.9682)	28.21	0.000

Source: Minitab ver. 16

Interpretation:

Since calculated z (28.21) is greater than the critical z (1.645), reject the null hypothesis (H₀) and accept the alternate (H₁). Therefore, there is a relationship between tax avoidance and evasion and aggressive accounting.

Hypothesis Two

H₁: The Nigerian tax system influence aggressive accounting

Descriptive Statistics: Hyp2

Variable	N	N*	Mean	SE Mean	StDev	Minimum	Q1	Median	Q3
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Hyp2	58	0	3.8391	0.0631	0.4806	3.0000	3.6667	3.6667	4.0000
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Variable Maximum

Hyp2	5.0000
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Source: Minitab ver. 16

One-Sample Z

Test of mu = 2.5 vs not = 2.5

The assumed standard deviation = 0.4806

N	Mean	SE Mean	95% CI	Z	P
58	3.8391	0.0631	(3.7154, 3.9628)	21.22	0.000

Source: Minitab ver. 16

Interpretation:

Since calculated z (21.22) is greater than the critical z (1.645), reject the null hypothesis (H_0) and accept the alternate (H_1). Therefore, the Nigerian tax system influences aggressive accounting.

Based on the above results and discussions the study captured the following major findings:

- There is a relationship between tax avoidance and evasion and aggressive accounting.
- The Nigerian tax system influences aggressive accounting.

Other Findings

- Respondents perceived that aggressive accounting practice in Nigerian manufacturing companies is done with the aim of manipulating share price, meeting external expectations by companies and achievement of internally set corporate goals..
- The loopholes in the legal regulatory framework of Nigerian tax system promote tax avoidance and encourage aggressive accounting in manufacturing companies
- Agency theory postulates the separation of ownership and control in corporations; Managers therefore in a bid to reduce the amount of tax manipulate the financial statement. This incidence can be reduced by strengthening the audit quality of Modern Corporation, e.g. employing the compulsory use of independent tax auditors in tax assessment.

3.4. Conclusion and Recommendations

The study finds out why companies evade and avoid taxes and suggested ways of minimizing the practice. The study established a relationship between tax avoidance and evasion as a sensitive factor influencing aggressive accounting practices in Nigeria. It also emphasized on the relationship between tax rates, and tax avoidance and tax evasion. The government should therefore embark upon public enlightenment campaign and adequate utilization of tax revenues on public goods to discourage tax avoidance; tax evasion and also the reduction in tax rate which have actually propel the activities of financial statement manipulations. This will certainly enhance and boost revenue generation in the country as is being pursue with vigour so as to survive in the present day economic meltdown, and inflationary setbacks. For Nigeria Government to meet up with its revenue targets especially now that the services of tax consultants have been discontinued it would be appropriate to take a look at the factors responsible for the incidence of tax evasion and avoidance since a check on these factors will go a long way in reducing if not eradicating the problem. Consequently, the paper recommended that:

- The legal regulatory bodies in Nigeria should devise measures to deal with the loopholes in the legal regulatory framework of Nigerian tax system and further that prominent accounting bodies such as ICAN and ANAN should also devise means of tackling accounting loopholes regulatory of Nigerian tax system.
- In the solution part of the creative accounting regularities, professional bodies should make a law which reduces the chances of alternative accounting methods. They should make the provisions of that if one company chose one method in good year it should choose same method in unfavorable year also.
- The tax authority should properly review and evaluate the assessment and collection procedures so as to encourage compliance by the taxpayers. The usual practice of reprinting parts of the tax laws and sending same to the taxpayers expecting that they would understand is not encouraging since these laws are written in legal jargons or terms that are not easily understood. Moreover, tax forms should be made less complex. Vast improvement can be made by improving the design of the forms. Since majority of the people are poor, tax evasion becomes inevitable. Government should therefore aggressively tackle the inflationary trend and also ensure that the poor pay very minimal tax.

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